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GOVERNOR

STATE OF MICHIGAN
OFFICE OF FINANCIAL AND INSURANCE SERVICES
DEPARTMENT OF LABOR & ECONOMIC GROWTH
KEITH W. COOLEY, DIRECTOR

KEN ROSS
ACTING COMMISSIONER

BILL ANALYSIS

BILL NUMBER:	House Bill 4677, as introduced
TOPIC:	Require annual audit of the Michigan Catastrophic Claims Association (MCCA)
SPONSOR:	Representative Lee Gonzales
CO-SPONSORS:	Representatives Richard LeBlanc, Michael Sak, Pam Byrnes, Hoon-Yung Hopgood, Mike Simpson, Dudley Spade, Kathy Angerer
COMMITTEE:	House Committee on Insurance
Analysis Done:	November 28, 2007

POSITION

The Office of Financial and Insurance Services (OFIS) supports this legislation.

PROBLEM/BACKGROUND

The Michigan Catastrophic Claims Association (MCCA) was established in 1978 and is a critical part of the no-fault automobile insurance system. Because there is no limit on the amount of coverage for personal injuries under a Michigan no-fault policy, the liability for this coverage would be too large for most individual insurers to bear. In other lines, when a liability is larger than an insurer can afford to accept on its own, the insurer transfers part of the risk to other insurers through a mechanism known as reinsurance -- insurance for an insurer.

Since the private market was not able to provide reinsurance for unlimited exposures without this special mechanism, the MCCA was created to act as the reinsurer to companies writing auto insurance in Michigan. As of July 1, 2007, each insurance company will pay the first $420,000 of any catastrophic claim and be reimbursed by the MCCA for the rest. This retention level gradually increases over the next 4 years until it reaches $500,000 in 2011. As the threshold increases, each insurance company assumes more of the risk for catastrophic claims. Any amounts over the threshold are paid by the MCCA and spread across all member companies in the form of the annual MCCA assessment.

Each year, the MCCA board of directors analyzes the amount needed to cover the lifetime claims of all people catastrophically injured in car accidents. This analysis includes an actuarial review of the MCCA's investment returns, surplus and liabilities, including medical cost inflation. This analysis yields an amount needed to pay those lifetime claims and may be adjusted to reflect excesses or deficiencies in earlier assessments. A per vehicle assessment is set for the year based on this amount. Each insurance company writing auto insurance is then assessed by the MCCA for each vehicle it insures. In effect, the MCCA acts as an insurer whose policyholders are Michigan automobile insurance companies. Insurance companies may pass the assessment on through the premium charged to policyholders.

This MCCA assessment has varied considerably over the years. In 1995, when the MCCA determined that its surplus was such that it could and should be reduced, it began applying a credit to the annual assessment amount. From 1995-2001 the MCCA returned approximately $267 per insured vehicle, in addition to a one-time lump sum payment of $180 in 1998 ($447 total per vehicle). Unfortunately, due to decreased investment returns and increasing medical costs, the MCCA's surplus is currently underfunded. For the period from July 1, 2007 through June 30, 2008, the MCCA Board will assess $123.15 per vehicle, which includes $106.63 in pure premium (the actual costs for current year expenses) and a $16.42 surplus/deficit adjustment (which reduces the shortfall in discounted reserves held for future obligations) and a $.10 administration fee.

Historically, the proponents of legislation requiring the appointment of an independent auditor to review the MCCA's operations have also sought to open the MCCA's operations to public accountability by also subjecting it to the Freedom of Information Act and Open Meetings Act as if it were a public agency.

Currently, the MCCA is annually required to file with the Commissioner a financial audit report from an independent audit firm. This report is available on the OFIS web site. The Commissioner also has authority to examine the affairs and operations of the MCCA at any time.

DESCRIPTION OF BILL

This proposed legislation would require the MCCA to submit to an annual audit by the Office of the Auditor General (OAG) or certified public accountant appointed by the OAG. The results of the audit would be reported to the legislature and would include a determination of whether the association will be able to meet its obligations.

SUMMARY OF ARGUMENTS

Pro

Requiring an entity other than the MCCA to select the independent auditor charged with reviewing its operations would presumably increase public confidence in the objectivity of the results of the audit.

In addition to determining whether the MCCA is likely to be able to continue to meet its obligations, an audit of its operations could assess a variety of non-financial aspects of the MCCA's performance, which wouldn't necessarily be reviewed by either the MCCA's annual financial audit. Passage of this legislation would represent incremental progress towards the goal of promoting greater transparency concerning MCCA operations, thereby increasing the level of public confidence in the critical function that it performs for the Michigan no-fault system.

Con

The OAG is responsible for periodically auditing state agencies. The OAG's expertise is in governmental accounting, not insurance company accounting. The MCCA uses statutory accounting principles (SAP), which are unique to the insurance industry. The OAG would have to acquire SAP expertise to make an annual determination on the MCCA's ability to meet its obligations. This would create additional cost in the current system.

The MCCA is already required to submit annual financial statements to OFIS, which include a detailed audit by a CPA firm, attesting to the MCCA's financial stability and internal control structure.

FISCAL/ECONOMIC IMPACT

OFIS has identified the following revenue or budgetary implications in the bill as follows:

(a) To the Office of Financial and Insurance Services:

Budgetary: None known.

Revenue:

Comments:

(b) To the Department of Labor and Economic Growth: None known.

Budgetary: None known.

Revenue:

Comments:

(c) To the State of Michigan:

Budgetary: The OAG would incur additional costs to adequately complete an audit of the MCCA.

Revenue:

Comments:

(d) To Local Governments within this State: None known.

Comments:

OTHER STATE DEPARTMENTS

The OAG would need to allocate additional resources to complete an audit of the MCCA. Given the technical nature of the business of the MCCA, the audit may require technical services that could be obtained only by contracting the services of an individual or firm with specific actuarial or insurance expertise.

ANY OTHER PERTINENT INFORMATION

This proposed legislation is similar to legislation introduced in previous and current legislative sessions.

ADMINISTRATIVE RULES IMPACT

This proposed legislation would amend the Michigan Insurance Code. The OFIS does have general rulemaking authority under the Insurance Code of 1956, 1956 PA 218.

Ken Ross
Acting Commissioner

11-27-07
Date